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DEPT FOR WHA/EPSC FAITH CORNEILLE

E.O. 12958: DECL: 10/21/2017
TAGS: EPET EINV ENRG ECON PREL EC
SUBJECT: GROWTH OF RESOURCE NATIONALISM IN ECUADOR

REF: A. STATE 150999

¶B. 06 QUITO 1722
¶C. QUITO 2277
¶D. 06 QUITO 1216
¶E. QUITO 2491

Classified By: Ambassador Linda Jewell, Reasons 1.4 (b&d)

¶1. (C) This cable is in response to reftel a asking for post's views on resource nationalism in Ecuador.

¶2. (C) In the petroleum sector, the GOE has taken a number of actions over the past year and a half resulting in increased revenues for the state. In 2006 under the previous administration, the GOE passed Law 42, an amendment to Ecuador's hydrocarbons law that requires that companies share at least 50 percent of "extraordinary revenues" with the state (Ref B). In October 2007, President Correa issued a decree that increased this percentage share for the state to 99 percent (Ref C). Following passage of the 99 percent decree, the GOE has agreed to renegotiate petroleum contracts with foreign oil companies (since all affected companies say the decree makes their operations untenable), but has said the gains for the state would have to match what the GOE would have received under the decree. Some consider that the decree is a way for the GOE to force companies to change from participation contracts to service contracts (where the companies would only be paid for services provided).

¶3. (C) In addition to new laws, the GOE has pursued legal actions against foreign companies that appear to be motivated by resource nationalism. In May 2006, the GOE issued a declaration of "caducity" and cancelled the contract of the largest petroleum operator in Ecuador at the time, U.S. company Occidental Petroleum, for allegedly illegally transferring ownership of assets to another company (Ref D). The GOE then seized the company's considerable assets in Ecuador and is now operating its former block. On November 1, 2007, the GOE issued a report detailing which foreign operators had not paid all of the money they owed under Law 42 and said it would actively pursue contract cancellation or seizing companies' oil as payment for this debt (none of the five foreign oil operators in Ecuador had paid all the GOE claimed they owed). Ecuador's state oil company Petroecuador then initiated a process to recommend caducity and contract cancellation for U.S. oil company City Oriente because it had not paid money owed under Law 42 of 2006 (Ref E). A final decision on caducity would need to be made by the Minister of

Petroleum and Mines, but company representatives appear resigned to eventual contract cancellation.

¶4. (C) Although there have not been any recent laws passed regarding mining, the Correa administration has said that mining would be a topic for discussion under Ecuador's soon-to-be-convened Constituent Assembly. Ecuador's Minister for Petroleum and Mines stated recently that the sector needs reform along the lines of the petroleum sector, with a much larger share of mining revenues for the state and greater government control. In spite of high commodity prices, investors have told us they are delaying any mining plans in Ecuador until there is more clarity in the rules governing the sector.

Comment:

¶5. (C) Actions to increase the GOE's control over natural resources have been increasing. The principal motivation appears to be increased revenues for the government. This has been mingled with a widespread and loosely defined nationalistic bent that believes that since the subsoil mineral rights belong the state, it is right and fair for the state to benefit from rising petroleum and mineral prices. However, we have not seen a particularly cohesive policy. Some GOE officials, as well as elements of the Ecuadorian business community, recognize the importance of private investment to develop Ecuador's mineral resources, and that the companies need a reasonable return and predictable business climate to do so. However, given the fractured nature of GOE policymaking, the government (across two administrations) has thus far not been willing or able to reach agreements with companies that would increase revenues for the state and also create a reasonable business environment for investors. For example, the Minister of Petroleum attempted to highlight in the press that it was pursuing "amicable" contract renegotiations with foreign oil companies, but then President Correa issued the 99 percent decree - a complete surprise to oil operators.

¶6. (C) Post considers that the USG cannot be out in front of the resource nationalism issue in Ecuador since we believe that doing so would back-fire, increasing nationalist sentiments and complicating the efforts of U.S. companies to secure negotiated settlements. However, we have and will continue to work the issue quietly behind the scenes, following the lead of affected companies. Post plans to continue to try to encourage the GOE to negotiate with companies rather than imposing decrees. We are also consulting with embassies and companies of other countries that are being affected by resource nationalism, so that we are not out in front of nations that now have a larger equity in Ecuador's petroleum and mining sector than the U.S. does, and so that we would be able, if appropriate, to coordinate actions with other embassies.

¶7. (C) We would like to suggest one area where Washington might be able to play a more proactive role in helping U.S. companies improve their public relations profile. At least in Ecuador, our view is that U.S. and other foreign companies have not done a good job explaining the benefits of their presence in country. This is a message that would be best if delivered across an industry and not by an individual company. Within Ecuador, companies usually operate independently and have difficulty reaching consensus on common actions within local business associations. Post recommends that Washington encourage broader U.S. associations, such as petroleum associations and other groups, to explain in the region the net benefits of the companies' presence. This message should include an emphasis on companies' corporate social responsibility programs, which are often robust and highly beneficial for the immediate community.
JEWELL